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In the Supreme Court

OF THE
United States

OCTOBER TERM, 1942

No. 392

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CHARLES ELWOOD CROPLEY
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STUART DAGGETT, SR., and AMERICAN
TRUST COMPANY, Executors of the
Last Will and Testament of Estelle
P. Clark, Deceased,

Petitioners,

VS.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

**PETITION FOR WRIT OF CERTIORARI
to the United States Circuit Court of Appeals
for the Ninth Circuit
and
BRIEF IN SUPPORT THEREOF.**

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vs.

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PETITION FOR WRIT OF CERTIORARI
to the United States Circuit Court of Appeals
for the Ninth Circuit.

*To the Honorable Harlan Fiske Stone, Chief Justice
of the United States, and to the Associate Justices
of the Supreme Court of the United States:*

Come now the petitioners above named and respectfully pray that a writ of certiorari issue to review the

Throughout, the italics in this Petition and Brief are ours.

judgment entered May 28, 1942 against them by the United States Circuit Court of Appeals for the Ninth Circuit. (R. 133.) The judgment was rendered on a petition to review the order of the Board of Tax Appeals which determined that the Commissioner of Internal Revenue properly assessed against Estelle P. Clark a deficiency of \$2365.00 of income taxes for the calendar year 1936 and of \$1149.15 for the part of the calendar year ending September 19, 1937, the date of the death of Estelle P. Clark. (R. 26.)

The judgment affirmed the order. Petition for rehearing was denied July 15, 1942. (R. 134.)

The judgment was by a divided court.

Daggett v. Commissioner of Int. Rev., 128 F.
(2d) 568;
R. 110 to 133.

The case was heard before the Board upon a stipulation of facts and accompanying exhibits.

Petitioners are the executors of the will of said decedent, having been appointed as such by the Superior Court of Alameda County, California. (Par. 9, Stip., R. 40.)

Each point relied on herein was carefully set out in the assignments of error contained in the petition for review filed in the Circuit Court of Appeals. (R. 33 to 36.)

SUMMARY STATEMENT OF THE CASE.

The case is an alimony trust case. It is our earnest contention that the recent case of *Pearce v. Commissioner*, U. S., 62 U. S. Ct. 754, 86 L. ed. Adv. Sheets 679 U. S., and the cases there considered were determinative. By a divided opinion, the Court ruled otherwise. Possibly it should be said that the majority opinion has restricted the scope of the *Pearce* case and the cases which it reviews by holding that although the income of an alimony trust is, under the facts, income of the husband prior to his death because it secures his contract to pay sums to his wife for her support, the death of the husband prevents a like holding as to any sums which his contract has made payable at a time which may be after his death, although the identical security arrangement was made effective so long as the payments were to be made. The Court may of course at once have in mind that the weekly payments which were to be made to the wife in the *Fuller* case were to continue for ten years and that the husband might have died the day after the divorce and that the guaranty of income which it discussed in the *Leonard* case was to be effective so long as the wife lived, which might exceed the husband's life. It would seem that the minority opinion is right.

The *Pearce* case shows that if a husband and wife make a separation agreement under which the husband creates a trust and grants to the wife the right to receive the income thereof for her support, the in-

come of the trust will be income of the husband under the following conditions:

1. If the husband guarantees the trust income will be certain amounts, the income is treated as security and as income of the husband and this is so although divorce follows and under the law of the state where the divorce is granted the Court loses jurisdiction to alter the payments.

2. If the agreement provides that the right of the wife to support is limited to the trust income, it is still income of the husband, if divorce follows and the jurisdiction mentioned is not lost. If such jurisdiction is lost, the right to the trust income is treated as a lump sum settlement and the husband is released. But mere contingent liability requires holding him liable for the tax on the income (if, of course, his total net income makes him subject to a tax).

3. If the trust remains largely in the husband's control and he retains a substantial interest in the trust corpus or its income, the trust income remains legally that of the husband.

The burden of proof is on the husband. The wife establishes the trust income must be taxed to the husband unless the husband clearly establishes the fact of release by local law and that he is not bound by contract and that the trust is not a trust in which he retains an interest and over which he has control.

The taxing of the trust income was governed by sections 161 to 167, inclusive, of the Revenue Act of 1936 (49 Stat. at L., pages 1706, 1707), the sections

now being sections 161 to 167 of the Internal Revenue Code, adopted February 10, 1939 (53 Stat. at L. 32). Section 167 of the Revenue Act of 1936 is headed "Income for Benefit of Grantor." Section 167-(b), Regulations 94, which section is set out under Section 167 of the Act of 1936, reads:

"* * * Such a distribution to the grantor occurs *if the income is paid to him or to another according to the grantor's direction* or, if, though paid to another pursuant to the terms of the trust, the benefit of the income inures to the grantor. The income so inures if it is or may be applied in satisfaction *of a legal obligation* of the grantor, does or may increase his net worth, does or may in any way enrich him, or does or may enable him in any way to enjoy, in substance, such income. Such a distribution also occurs if the income is applied in payment of premiums upon policies of insurance on the grantor's life." (Italics ours.)

Section 19.167-1(b) of Regulations 103, set out under section 167 of the Code, reads:

"Thus, the inclusion of any trust within the scope of section 167 is based on the fact that the grantor has retained an interest in the income therefrom by which he is, or may be enabled at some time, to receive its benefits. But the provisions of section 167 are not to be regarded as excluding from taxation to the grantor the income of other trusts, not specified therein, in which the grantor is, for the purposes of the Internal Revenue Code, similarly regarded as remaining in substance the owner of the trust income. If, for example, trust income is applied in satisfaction of the grantor's legal obligation *whether to pay*

a debt, to support dependents, to pay alimony, to furnish maintenance and support, or otherwise, such income is in all cases taxable to the grantor."

Section 162 of the Act of 1936 is identical with Section 162 of the code. Subdivision (b) of the section prescribes that where the income of a trust is regularly distributable to a beneficiary such income is not taxable to the trust as a person but the same is merely included in the gross income of the distributee. Thus a distinction is drawn between the taxing of such income and the taxing to the trustee of income that is the result of accumulations or the result of capital gains. Application by the trustor of such income to the payment of his debts equals the receipt of it by him. Regulations 94, Article 162-1(3) contain the following:

"Any income of an estate or trust for its taxable year which during that year may be used, pursuant to the terms of the will or trust instrument, in the discharge or satisfaction, in whole or in part, of a legal obligation of any person is, to the extent so used, taxable to such person as though directly distributed to him as a beneficiary."

This identical language is found in Regulations 103, Sec. 19.162-1(3).

The regulations are clear that a wife who receives support payments does not receive income. The husband can not deduct the payments. We quote:

"* * * and an allowance paid under a separation agreement are not deductible from gross income."

Reg. 103, Sec. 1924-1; Sec. 1922 (b) (3)-1.

The said majority opinion shows, and in this case it will be conceded, that the separation agreement involved provided for payments by the husband to the wife for her support *for life*; that the husband set up a trust the income of which was to secure these payments, that the husband guaranteed the payments would be a specified amount annually; that divorce was granted and that the divorce Court lost jurisdiction over the subject of alimony; that the *agreement recited that the payments to be made to the wife were what should be adjudicated in her favor, for her support*; that a judgment was obtained on the wife's behalf establishing that and establishing that the contract bound the former husband's estate; that this judgment determined the trustee was entitled to recover from the husband's estate an income deficiency of \$4040.06 for the fiscal year of the trust, July 7, 1935 to July 7, 1936, and that this judgment became final. This judgment embraced a period after the husband died, for he died on December 9, 1935. The government has not so much as suggested that this money was the wife's income. It will be conceded that in these respects the case originally came within the first class above. We urge that it was also within the third class, although we believe it will not be necessary to consider that point. But the Court by its majority opinion ruled that as the husband died on December 9, 1935, the trust income in question between that date and September 19, 1937, the date of the death of the wife, was income of the wife.

While the majority opinion states that the estate of the ex-husband would be liable only for *deficiency*

in trust income and seemingly suggests that for that reason the income was not security, the distinction is in view of the *Leonard* case, clearly groundless. Moreover if such was the law the wife would always be held for the tax in those jurisdictions such as California where security must be exhausted before seeking to hold the debtor. (217 Cal. 644, 20 Pac. (2d) 940.) Equitably such a distinction is groundless. If the creditor must otherwise satisfy the debt, he uses up an equal amount of property. If the point were good, it should have been applied in the 23 years that preceded the husband's death. The deficiency assessment letter shows that prior to December 9, 1935 the trust income was assessed to the husband. (R. 14 and 15.)

Whatsoever the reasoning of the said majority opinion may be the actual basis of the opinion is and can only be the argument that death of a husband does of necessity terminate the obligation of a husband to support his wife. Death does do that as to what might be called the involuntary obligation that rests on the duty created by law when the husband marries and which may continue to be enforceable by a divorce Court while the husband lives.

But the agreement here involved presents a different duty; a duty imposed by contract. It was a pre-divorce agreement intended to apply even if the marital relation was dissolved and the single status of the parties restored. The right to the legal type of alimony which is supposed to be continuously adapted by the Court to the capacity of a living husband to pay and to the

needs of the wife was destroyed, but it was superseded by a self-imposed duty. *The duty was founded on a legal consideration.* When such a contract is made, it is regarded as a permissible contractual assumption by the husband of a duty to support. It is elementary that the payments which such a contract provides for a wife's support need not be as a Court would prescribe in an alimony case. The surrendered right "to bed and board" within the home is alone sufficient for what the husband agrees to pay for support. It is elementary that these support obligations, although based on mere agreement, have enjoyed a preferred status both under the income tax law and the bankruptcy act. They can not be discharged in bankruptcy. They are not taxed to the wife. They represent personal expense not deductible from the husband's income. Amounts unpaid under the contract would no more be credits against income of an estate than would the unpaid part of strict alimony payments that remain a claim against an estate. (10 Corpus Juris, 1075, 1076). *It is certainly elementary in bankruptcy law that if the payments agreed to be made for support happen to fall due after the death of the wife or after the death of the husband they are still support payments. At no time will discharge in bankruptcy affect them. That is determined in New York where the contract here involved was made.* (See pages 47-48 of the Brief attached.) The husband can not be imprisoned for breach of the new duty. It is a personal obligation but it is in no sense a personal service obligation. It can not be enforced except against property. But it can be so enforced against property either before

or after the husband dies. As to the effective after death remedies in such a case, see pages 55-58 of the Brief.

In any event the majority opinion is basically erroneous. It concedes that in any event the liability persisted. In fact a judgment for income deficiency was obtained on this contract after the husband died. The sole conceivable reason for discussing the character of payments intended for support which, in view of the events that transpire, happen to fall due beyond the joint lives of the spouses is the argument that the quality of the payments is lost if either spouse dies so that the balance of the payments suddenly represent a purchased annuity. However the case of *Helvering v. Butterworth*, 290 U.S. 365, 78 L. ed 365 seems to indicate that a person is not to be deemed a purchaser of an annuity unless the price is ascertainable by some standard.

The Government does not aim to tax any part of an annuity that is not profit. The provision for taxing annually so much of the annuity payment as equals 3% of the aggregate premiums or consideration is merely a means of insuring the taxing of possible profit. While the law formerly prevented taxing any part of annuity payments until the cost was returned, the taxing of the small percentage referred to is now permitted. (Sec. 22 (b)(2) Rev. Act, 1936; 49 Stat. at L. 1667.) There is no profit at all in annuity payments which but equal the price. Here Mrs. Clark lived less than two years after the husband died. He died December 9, 1935 and she died September 19,

1937 and we are concerned with the year 1936 and a part of the year 1937 and the possibility of argument that there was a purchase of an annuity payable to Mrs. Clark in the year 1936 and in the fraction of the year 1937. If we assume that the tables used by insurance companies gave to Mrs. Clark a life expectancy beyond the life of the husband of about two years, the charge for the annuity would probably have been about what Mrs. Clark received in the way of payments plus something for overhead. The legal situation thus created would mean that instead of trying to tax the whole of the payments made to Mrs. Clark the Government would be confined to taxing approximately 3% thereof and indeed that might be excessive. It would be entirely unfair for the Government to try to shift its theory simply to enforce payment of an utterly unfair tax. It taxed this income as income of an ordinary trust. (R. 17.)

It would seem the height of unreason and unfairness to say that the indulgence of the wife in deferring payment of certain sums for her support, or her doing that because the husband is in need of his funds and she is possibly temporarily otherwise provided for, his death or her death penalizes her and makes her pay taxes on income of a trust designed to secure the payments. The husband says to the wife: "Grant me ten days time to make one of the fixed payments for support." They so agree in writing, and thus make a legal change in their contract. The wife dies before the time is up. The opinion below means the payment has become gross income of the wife's estate. In the at-

tached brief we shall show that in New York it has been explicitly ruled that where in the separation agreement the parties—as here—recited the stipulated payments would be for support, it is immaterial that they happen to fall due after the joint lives of the parties and we shall additionally show that sanction for these rulings is found in a declaration in one Supreme Court case and in a ruling in another. The cases show that payments so agreed upon can not be discharged in bankruptcy because they are justly support payments. The attached brief will also bear on the elementary rule that death does not destroy a contract that is not for personal service or convert into ownership that which is security. It will answer, to any extent not herein answered, the point made in the majority opinion below that if in the agreement the wife waived her dower right or received a power of appointment makes a different case. But we may mention at once that the majority opinion failed to note that dower was waived in *Douglas v. Willcuts* and that a power to appoint was granted to the wife in the *Fuller* case. It failed to note that a power of appointment is not property and has no market value whatever. May we state respectfully that for 23 years the objections last mentioned remained undiscovered by the husband or by the Government. It failed to note that if the power was property, the grant of it probably reduced the support payments.

In *Douglas v. Willcuts*, 296 U. S. 1, 80 L. ed. 3, the Supreme Court refused to render the contract or the decree ineffective by saying that the regular payments

called for settled property rights. The decree was that the payments were "in lieu of all other alimony *or* property or estate of the defendant." Said the Court:

"However designated, it was a provision for annual payments to serve the purpose of alimony, that is to assure to the wife suitable support. The fact that the provision was to be in lieu of any other interest in the husband's property did not affect the essential quality of these payments."

Under New York law neither husband nor wife had in 1906 an inheritance right in property of the other. The wife here waived her contingent right of dower. The husband waived his right of curtesy. So the wife stripped herself. These contracts would be of little worth as against bankruptcy, if the Court is to hold they may not settle property rights *and* provide for support. (Civil Code Cal. Sec. 159 is in the conjunctive.) If the right of support is lost because there is some sort of surrender, why not defeat the contract by argument that the home, the shelter and the conveniences surrendered by the wife were worth but half what the husband is to pay. The right way is to say, as the Government for 23 years must have said, that waiver of dower balanced waiver of curtesy. In any event, the law lets the parties agree what is fair for support in the up-set life that follows separation and they should not be permitted to deny their contract. Support, possible illness—all kinds of contingencies must be considered and judged. In the *Rider* case mentioned in the attached brief, the Court held the separation contract was a support contract *in the ab-*

sence of any showing as to the extent that settlement of a breach of promise claim influenced the payments. So, if there is anything in the point, the burden is on the husband to make out the claim.

In the *Tilles* case dower was waived. It is fair to state that such waiver is probably common to these contracts.

If there was any doubt about considering these contracts as containing a separate adequately supported provision for support, where no question of good faith can be raised under the evidence, *Douglas v. Willcuts* settles that. In the New York case cited at page 48, and in which it was held the payments that might be made after the wife died would be support and were not dischargeable in bankruptcy, the husband had received property from the wife and such was the *Tilles* case.

If the Court starts the journey from the explicit agreement, it could not only speculate as to what the right of the wife 30 years later, if she survived, to use a piece of real property would be, but it could also speculate as to what additional real property the husband might have acquired. The law is not so impractical. It would certainly seem utterly unfair to simply subtract an attempted valuation of dower from the total of what the wife receives. That legally gets nowhere. If valuing is to be done and the claim is that some part of a payment intended strictly for support is not support, the Court has the impossible task of determining, as of the date of the agreement, what in

dollars and cents the value of "bed and board" would have been which the wife had the right to by virtue of the marital relation. There are now 50 departments of the Superior Court in Los Angeles. Each judge has divorce jurisdiction. Were these judges to act independently on a divorce case of the same facts, the result would probably be a mass of different decisions as to what the proper amount of alimony should be. One judge might say that he believed the wife was in ill-health and had no earning capacity and another might attach little weight to the evidence on this point. One might have said, in the very type of case here presented, that, in view of the wealth of the husband and his earning capacity or income and the station in life of the parties, the sum of \$30,000.00 annually would be proper support for the wife. Whether if dower was waived, the awarded payments would not have been more or less is mere surmise.

The point is that the law permits settlement of property rights in the agreement and also the making of provision for the wife's support.

What is dower measured as of February 28, 1906? Apparently in condemnation cases, it would present this kind of estimating. Consider such a sum as would if put at interest on February 28, 1906, produce the rental value of a third (or the legal fraction) of Mr. Clark's real estate from December 9, 1935 to September 19, 1937. But the wife would not immediately get this because the right is contingent. It would be impounded and if she died first or the law abolished dower, it would be the husband's property. The valua-

tion expert might have to consider deterioration or at least obsolescence. If the tables show the husband will outlive the wife, it would seem the valuation would be zero. But this does not end it. The husband waives curtesy which involves off-set. It would seem that it would here have involved subtracting one flea-bite from another flea-bite. Or looking at the thing from the other end this would be the situation. The wife has received \$25,000.00 annually for about thirty years. Assume there was some real property that existed on February 28, 1906. Compare the money with use of the real property for about two years, noting that—to balance—the payments would be considered as drawing interest for an average of fifteen years. At 4%, that would mean interest totalling 60% of \$750,000.00 which would have to be added to the \$750,000.00, the total of the payments, to balance.

The law accords the privilege of agreeing on support and it does not presuppose that the Commissioner of Internal Revenue or a bankruptcy court shall go back thirty years and try to determine what a divorce court would in the subsequent period have allowed to the wife for support.

We shall first state the facts very generally and then explain the rulings in the alimony trust cases which bear on those facts so as to bring out the points involved. We shall then quote from the contract and from a judgment obtained on that contract, showing the payments were for support.

OUTLINE OF FACTS.

On February 28, 1906, James F. A. Clark and Estelle P. Clark were husband and wife residing in New York. They there made a separation agreement bearing said date which was intended to provide the wife \$25,000.00 annually for her support. The parties had an adopted daughter who was a minor eight years old. The wife agreed to care for and support the child during its minority or until its marriage, if it married before becoming of age. The contract failed to provide for any payments directly for the child's benefit. It ended at the death of the wife. In the agreement the husband transferred a large amount of securities to Colonial Trust Company of New York as trustee and authorized the trustee to collect the income from the securities and to pay it—to the extent of \$25,000.00 annually—to the wife for her support during her life. (If the wife obtained a divorce and remarried, the payments were reduced to \$15,000.00 annually. She obtained a divorce. She did not remarry.) The husband guaranteed the income would be \$25,000.00 annually. Excess income was payable to the husband. If securities defaulted as to income, the husband was required to substitute paying securities. The husband expressly agreed the contract would be binding on his estate. A final judgment (hereafter mentioned) was obtained by the trustee after the death of James F. A. Clark determining that the contract was binding on his estate. This judgment required the estate to make up a deficiency in income of \$4040.06 for the year ending July 7, 1936.

Investments in the trust could be changed only with the husband's consent. Subject only to the wife's

testamentary power to appoint a part of the property in the trust, the reversionary interest in the trust was retained by the trustor.

The wife waived dower. (Par. Eleventh, R. 53.)
The husband waived curtesy. (Par. Twelfth, R. 54.)

The District Court of Lincoln County, South Dakota, granted the wife an absolute divorce on October 1, 1906, the decree reciting "Ordered, * * * that no allowance be made to plaintiff for alimony, support or maintenance" and that it should not be subject to future modification. (R. 60, top of page.) It is conceded this decree was final in this respect.

The Contract Was Valid for the Life of the Wife.

Time and again it has been ruled in New York that *the parties may distribute the payments agreed to be made by the husband to the wife for her support so that part will be payable after death*, that with the consent of the husband an alimony decree may so provide.

Babcock v. Babcock, 147 Misc. 900, 265 N.Y.S. 470;

In re Tashenberg's Estate, 149 Misc. 124, 267 N.Y.S. 502.

This is the law generally and the Federal Courts would be forced to recognize the state rule on this point if the law were not general.

Whitney v. Whitney Elevator & Warehouse Co.,
180 Fed. 187, 106 C.C.A. 28 (cert. den. 219
U.S. 588, 55 L. ed 348).

Rulings Already Made on Contracts that Ran Beyond Period During Which Alimony Might be Awarded.

We earnestly contend that by its denial of certiorari in the *Alsop* case and by its denial of the writ in *Barbour v. Commissioner* (which involved the same point as did the *Glendinning* case and the *Weir* case) this Court meant to make income from such a security trust as that which is here involved income of the husband, and that it is immaterial that times of payment called for by his agreement are in a period when, had jurisdiction of a divorce court been originally exercised or retained, payment would not have been or could not have been required.

In the *Alsop* case the husband's agreement was to make the support payments *for the life of the wife*. She remarried and the argument was that as alimony could not be made payable after the wife remarried, the trust income was the wife's. But the Court ruled that the *agreement* bound the husband, and the Court in this case has erroneously said the case is not in point. But the Court there said:

"Whatever this agreement may be called, 'a family settlement' or anything else, it was in lieu of alimony *for her entire life*."

Alsop v. Commissioner of Internal Revenue, 92 Fed. (2d) 149, 150 (certiorari denied Jan. 31, 1938, 302 U.S. 767, 82 L. ed. 595).

The following case clearly approves precisely the ruling of the *Alsop* case and cites as in harmony this Court's ruling in *Helvering v. Corey*, 297 U.S. 694, 80

L. ed. 986, which was made on the authority of *Douglas v. Willcuts* and the cases which followed.

Donelley v. Commissioner, 101 F. (2d) 879, 882.

In *Glendinning v. Commissioner*, 97 Fed. (2d) 51, it appeared that under the laws of Pennsylvania the husband could not by Court decree be obligated to pay anything to his wife, after divorce, as support and maintenance. However, prior to the decree which the husband obtained, the husband created a trust, in which he became obligated to pay the wife an annual *sum for life* for her support. He, under the contract, remained personally liable. It was in effect ruled that the trust was created as a substitute for a Court order for support *that could have been made effective prior to the divorce*. The husband was held liable for tax upon the payments resulting from the trust, the Court stating in part at page 52, "but the income from a trust fund put up to meet an obligation of the creator of the trust, is the income of the debtor."

The ruling in the latter case was followed on the second question decided (which we have explained) in

Weir v. Commissioner, 109 Fed. (2d) 996.

In *Barbour v. Commissioner*, 110 F. (2d) 660, it was stated *that the question involved was identical with the second question decided in the Weir case*, and in *Barbour v. Commissioner*, certiorari was denied. (310 U.S. 682, 84 L. ed. 1399, 60 S. Ct. 976.)

In the following case the husband agreed in a pre-divorce separation agreement to make payments to the wife for her support *for life*. The husband obtained

the divorcee. It was admitted that the Missouri divorce Court could not have awarded alimony to the wife if the husband obtained the divorce. To secure the payments a pledge of securities was created. *The wife had transferred securities to the husband. She waived her dower rights.* The question was as to whether income of the pledge accruing in 1931 was the husband's income. It was held that when the separation agreement was made—which was before the divorce—he could contract to support his wife for life. It was held that the income from the pledge was taxable to the husband. Seemingly to make an end of the controversy, the Court, after a review of the alimony trust cases, said explicitly that the contract would have the same effect if the husband should die or if the wife remarried.

Tilles v. Commissioner of Int. Rev., 113 F. (2d) 907.

And certiorari was denied in this case:

311 U. S. 703, 85 L. ed. 456, 61 S. Ct. 59.

The following is a summary of the alimony trust or separation cases in which the husband distributed his obligation over a period beyond his life. That is, he measured his obligation by the life of the wife, or by a period that might extend beyond the husband's life. Kindly note that we have:

(Cases determined here.)

1. In *Douglas v. Willcuts*, a contract for life.
2. In *Helvering v. Leonard*, a contract for life.
3. In the *Fuller* case, a contract for a definite term which might exceed the husband's life.

4. In *Pearce v. Commissioner*, a contract for life.

(Lower Court cases.)

(a) In the *Alsop* case, a contract for life.

(b) In the *Weir* case, a contract for life.

(c) In the *Glendinning* case, a contract for life.

(d) In the *Tilles* case, a contract for life.

Further as to Foundation of Ruling Below.

The only justification for the lower Court's ruling is the decision in the *Thomas* case (100 Fed. (2d) 408). In that case the husband had died. While that case might possibly be said to involve features of an alimony trust case, the facts were so complicated that the Board of Tax Appeals did not cite it. (R. 22 to 26.) There was a compromise after the husband and wife made their original contract. It could be argued that the payments to be made to the wife lost their identity as support payments. Certainly this case was the first case to treat it as a precedent which should be followed here. There was first an opinion by Judge Augustus Hand. That opinion suggests possibly that the parties must have agreed that waiver by the wife of her dower right had constituted the consideration for the alimony payments made after death, because—it was argued—the right of the wife to claim support from the husband ceases at death. It must be conceded that any such allocation of consideration as that would be fiction; that there was nothing in the contract that justified that.

In the *Thomas* case Judge L. Hand wrote an opinion in which he justified taxing the wife on the income after death of the husband as a matter of convenience. His opinion said:

“If it were practicable to continue the tax upon his estate after his death, I should therefore think that was the proper way * * * he has given a quid pro quo measured by a less sum for a longer period.”

Judge L. Hand had to say that in view of his opinion in the *Adams* case, a bankruptcy case, cited in the appended brief.

Possibly Judge L. Hand had the view that is suggested in the majority opinion here, that the law aimed to tax the income of an alimony trust as to a separate person. There is no such intent. Whether there will be a tax as well as the amount of the tax will depend on the remaining income and the credits and deductions of the husband. Income that is distributable annually is merely the income of the recipients thereof. The trust is taxed as a separate entity only as to capital gains and income accumulations.

To the argument of convenience made by Judge L. Hand there are two answers:

FIRST: In view of the fact that the law and the regulations explicitly sanction creating a trust the income of which secures the promise to pay of any debtor, the argument leads to absurdity. It obviously is not the law that if the creditor is a bank or lending institution, death of the debtor will shift the tax and

require counting the trust income as a part of the income of the creditor.

SECONDLY: The inconvenience is no different from that which results from death of debtors in other cases. Never is the effect of the passing of the debtor's estate the same in two cases. Increase or decrease in taxable income may result. That the inconvenience produced by the type of case has some special features is no reason for telling a bank or an ex-wife that death has converted that which was security into absolute ownership.

(The first answer is sufficient and we trust that the argument with respect to the second will not be treated as an apology for the first. There is no apology for the first, even if the conclusion should mean loss in taxes.)

Note what happens when the rich parent dies. He pays a heavy income tax. So does his estate. The law declares his estate is a person; likewise a trust; likewise a partnership. (Internal Revenue Code, Sec. 3797.) But the trust is not taxed as a person except to a limited extent; the partnership not at all. The estate is taxed as a person during administration. The decedent may leave a dozen children; he may will his property to forty people. The identical amount of income from the identical property may pay no tax at all.

The sole disturbance is: What happens to the fine set-up if the rich ex-husband who has created an alimony trust which secures his continuing obligation happens to die? It may be argued that income com-

mitted to the payment of the debtor's debt, whether it be from a trust in personalty or from a mortgage of crops on real property or from a pledge of personal property remains income of the debtor if he lives, even if he, by a sale or gift, parts with the entire equity in the property the use of which is so committed—this upon some theory that creating the debt and the security was some sort of an irrevocable commitment of the income, something that made it unalterably a particular item of gross income of a particular debtor, even though title to what produced the income passed; that forever or until the debt is paid that income must always show up in the gross income of the original debtor.

Having in mind that the fact that any trust is, in so far as the rights of the trustor are concerned, just as alienable as are the rights of a mortgagor or a pledgor, the theory last mentioned would seem to be entirely unsound or that the law has inadvertently created a freakish result in a case because the security is trust income. Obviously a mortgage of crops extending for several years or a pledge of income of securities would cover income only.

If in his lifetime the trustor by a transfer in good faith divested himself of the residuary interest in a trust set up as security or if he was divested by execution or bankruptcy of that interest, it would seem clear that the person who acquired the encumbered property would count the entire income therefrom in his gross income. *He could not claim as a deduction or as current expense, the amounts which the income an-*

nually retired in relieving the property of the encumbrance because that would be improvement of his position and in the nature of a capital disbursement. That would be considered equivalent to buying the title; equivalent to succession to a title being acquired under contract to purchase.

Suppose the debtor dies and the encumbered property passes by will or inheritance. Death creates complication for the creditor as well as the government. Where the claim is contingent the creditor can (as is frequently done) ask to have impounded enough of the estate to make reasonably certain the contingent claim will be paid. The equity in the deposit and the balance of the estate goes to the heirs or as the will provides.

But says the Government: Who would want the trustor-interest in a trust in a large amount of assets when annually the income from those assets might be largely taken to pay a debt of the decedent. Of course, it is the law that what a will gives may or may not be accepted. But that alters not the slightest the rights of the creditor, Estelle P. Clark. It is just one of those situations which death and not her act has created. We have diligently sought an express answer in the income tax law and the cases to the question: Must the devisee who takes land heavily mortgaged or the income of which is hypothecated for years (which is practically the same thing) report the yield therefrom as a part of his gross income? We find no exact precedent, but we believe the answer

is "Yes" and that there is no real hardship. The income is virtually buying the place by paying the charge down to zero and the payments out of income would not be a deductible by the devisee.

Section 22 of the Internal Revenue Code says that gifts under a will are not income but that yield therefrom is income and would be rational to say such yield is income of the beneficiary although it goes to a creditor, if the payments purge the title.

The value of the assets in this trust plus cash were over \$400,000 at Mrs. Clark's death. So at least in this case there would not, in view of the wife's probable age, be hesitancy to accept the trust estate.

Why create a tax against the ex-wife or a lending institution, simply because the promisor has died?

This contract was made in good faith before we had an income tax law. *If Congress desires to have alimony trusts taxed as a unit or if Congress desires to have security trusts taxed as a unit, it should be done by a new law, and not by Court decision. It does not tax to the trustee income which is distributable.*

Note Regulations 94, Article 162-1 (3) and present Regulations 103, Sec. 19.162-1(3) hereinbefore quoted.

The present regulations declare:

"Interest paid by the taxpayer on a mortgage upon real estate of which he is the legal or equitable owner even though the taxpayer is not directly liable upon the bond or note secured by such

mortgage may be deducted as interest on his indebtedness."

Regulations 103, Art. 19, 23-b-1.

Note the reference was to *interest* only.

This court has stated that the income tax law is to be construed as intending to tax what amounts to income within any of the defined categories. (*Helvering v. Clifford*, 309 U.S. 331, 84 L. ed. 788.) So it could be urged that the income from the legacy charged with an obligation would be included in the income of the legatee.

We now deal with the *Pearce* case which is cited in both opinions below. (Probably the *Leonard* case should be stressed because the opinion in that case meets the statement in the majority opinion that all Mr. Clark or his estate did was to guarantee against income deficiencies.)

We may first mention *Douglas v. Willcuts*, 296 U. S. 1, 80 L. ed. 3, as the *Pearce* case opens with a reference to that case. There the husband made an agreement immediately preceding the entry of the divorce decree by the Minnesota court, in which he undertook to pay to his wife fixed payments *for life*—the sum of \$15,000.00 up to November 6, 1927 and thereafter \$21,000.00 annually. *The wife waived her dower right*. It was agreed that the support payments would be secured through income of a trust. Excess income went to the husband in case principal was not impaired. Deficiencies were to be made up in a prescribed manner by the husband. The contract recited that it "was in

lieu of any and all claims for support, maintenance and allowance for her support". (Such is the contract here.)

The decree of divorce adjudged that the trust should be set up and that its provisions should be *in lieu of alimony and the wife's interest in the property or the estate of the defendant*. The Court ruled that it could not be said that the divorce court had not allowed alimony or that its jurisdiction was lost. It held that the trust income secured the continuing obligation of the husband to make payments to his wife, that it was used *to serve a purpose of the husband*, and was his income. It quoted from the *Butterworth* case, as follows:

"The court observed that 'evident general purpose of the statute was to tax in some way the whole income of all trust estates'."

Now, of course, this statement last mentioned, which is mentioned in the majority opinion below, was not intended by the Supreme Court to be taken in a literal sense. The husband, might not have been taxed a penny on this trust income. It had to be counted as a part of his gross income and his deductions might have left no tax whatsoever.

In the *Pearce* case, the husband agreed in writing to pay his wife \$500.00 a month *for the rest of her life*. The wife obtained an absolute divorce under Texas law in the year 1917. The decree was silent on the question of alimony. The contract reserved to the husband the right to substitute for his obligation an

annuity contract. Following the divorce, he provided the wife with the annuity. The Circuit Court of Appeals held that it was not enough for the wife to show that under the Texas law the divorce court *might* have power to change the decree; that to overcome the Commissioner's ruling it was essential that the wife should establish that the law was clear on this point. The Supreme Court granted a review because of the standard applied. It held *that the burden in these cases is in the main on the husband*. It said:

"We do not think that that was a correct application of the *Fitch* or *Leonard* cases. Those cases hold that the income is taxable to the former husband, not only where it is clear that payments to his ex-wife were made pursuant to a continuing liability *created by his contract or by local law, but also where his undertaking or local law makes that question doubtful or uncertain.*"

But the Court held that even within this favorable rule the wife had not made out a case.

The Court then explained exactly what it had ruled in the *Fitch* case, the *Fuller* case and the *Leonard* case.

1. It said that the *Fitch* case determined that while the wife's right to income from the alimony trust purported to be limited to \$600.00 a month and there was no guaranty of the income by the husband, yet he had not shown that the Iowa divorce court could not change the amounts payable by him. (*Helvering v. Fitch*, 309 U. S. 149, 84 L. ed. 665.)

2. It said it had made the same ruling in the *Leonard* case. There, as will be shown, the husband had, as here, guaranteed income from certain securities which income went to the wife for life. And on that ground *also* it was ruled the husband was held as to part of the payments. (*Helvering v. Leonard*, 310 U. S. 80, 84 L. ed. 1087.)

3. The Court then dealt with the *Fuller* case. (*Helvering v. Fuller*, 310 U. S. 69, 84 L. ed. 1082.) There certain support payments were to be made during a definite term, which of course, might exceed the life of the wife. Unguaranteed income of a trust was to be paid to the wife for a like period. The Court said:

"In the *Fuller* case it was clear under Nevada law that the court retained no control over the divorce decree which approved the trust settlement. Since there was no such reserved power and since the trust contained no contractual undertaking by the husband for support of the wife, we concluded that his obligation to support had been pro tanto discharged. We held, however, that the husband was taxable on a \$40 weekly payment which he had agreed to make to his wife. But that fact did not make him taxable on income from the trust also, since the provision for weekly payments and the trust 'were not so interrelated or interdependent as to make the trust a security for the weekly payments'. 310 U. S. p. 73, 84 L. ed. 1084, 60 S. Ct. 784. We also noted (p. 76) that though 'the divorce decree extinguishes the husband's pre-existing duty to support the wife, and though no provision of the trust agreement places such obligation on him that the agreement may

nevertheless leave him with sufficient interest in or control over the trust as to make him the owner of the corpus for the purpose of the Federal Income tax under *Helvering v. Clifford*, 309 U. S. 331, 84 L. ed. 788, 60 S. Ct. 554'.

Thus a property settlement made for the purpose of maintaining or supporting the wife may be treated for income tax purposes as mere *security* for the husband's continuing obligation dependent on such consideration as whether it contains, *or* is interrelated with, contractual obligations of the husband for her support; whether the court has a reserved power to alter or modify it; *or* whether the husband retains any substantial interest in the property conveyed. Where the settlement carries some of the earmarks of a security device, then the power of the court to add to the husband's personal obligations may be especially significant. See *Helvering v. Leonard*, 310 U. S. 80, 84 L. ed. 1087, 60 S. Ct. 780, *supra*. But where, as here, the settlement appears to be absolute and outright and on its face vests in the wife the indicia of complete ownership, it will be treated as that which it purports to be in absence of evidence that it was only a security device for the husband's continuing obligation to support."

Pearce v. Commissioner, 62 U. S. Ct. 754, 86 L. ed. Adv. Sheets 679.

The *Pearce* case is not a full summary of the part of the *Leonard* case which is the same as this case. There, as here, Leonard, the former husband, guaranteed that certain securities placed by him in an alimony trust would yield certain amounts *for the life* of his wife. And it is the part of the decision that

relates to this special provision which is so obviously in point here. There the agreement involved:

1. Putting \$650,000.00 in a trust of which \$400,000.00 were 6% bonds.

2. Guaranty of payment of the interest on those \$400,000.00 in bonds for the wife's support *for life*.

3. If the total trust income fell below \$65,000.00, the husband was to make up the deficiency but under specified contingencies, this could be limited to \$55,000.00.

The Commissioner, Helvering, lost out below, the Board and the Court ruling; *first*, that it was not a security arrangement at all, and *second*, that the Court lost divorce jurisdiction to change the contract. The Commissioner appealed. Both grounds were overruled.

The Supreme Court first proceeded to single out the guaranty and explicitly ruled that the guaranty of payment of the 6% interest on the \$400,000.00 in bonds was taxable to Leonard because to that extent at least the agreement created a debtor-creditor-security arrangement. Said the Court:

"For *these reasons* that portion of the trust income which was received from the guaranteed bonds was clearly taxable to respondent."

The Court further said:

"Hence the case in substance is the same as those where pursuant to contract or arrangement an obligation is discharged by another for the tax-

payer's benefit; see *Old Colony Trust Co. v. Commissioner of Internal Revenue*, 279 U. S. 716, 73 L. ed. 918, 49 S. Ct. 499; *United States v. Boston & M. R. Co.*, 279 U. S. 732, 73 L. ed. 929, 49 S. Ct. 505; or where the taxpayer creates a trust, the income of which is applied to the discharge of his debt. See *Helvering v. Blumenthal*, 296 U. S. 552, 80 L. ed. 390, 56 S. Ct. 305. Here, as there, the taxpayer received a benefit by the payments."

Helvering v. Leonard, 310 U. S. 80, 84 L. ed. 1087.

(We wish to mention that Judge L. Hand participated in the erroneous ruling below and this is some indication of a mistaken notion on his part as to the nature of these cases.)

Leonard did not agree to make the payments of \$24,000.00 annually. But as here, he guaranteed them. Here Mr. Clark agreed for himself and his estate to guarantee them. (Par. Third, R. 46.) Mr. Clark agreed to put good securities in the trust for bad. (Par. Sixth, R. 51.) Under Par. Tenth (R. 53) Mr. Clark was clearly the person responsible for investments. He was the one to change securities although this was to be with the approval of the trustee or Mrs. Clark. The trustee assumed no responsibility for investments. (Par. Fifteenth, R. 55.) By express terms the agreement was binding on the decedent's estate or legal representatives. (Par. Nineteenth, R. 57.)

We now make more specific references to the record and the agreement in order to establish each fact asserted.

When James F. A. Clark and Estelle P. Clark made their contract dated February 28, 1906, they resided in New York. (Item 1, R. 38.)

Extracts from agreement:

"* * * and the party of the first part is willing to provide for the support of his wife and child, so as to avoid proceedings against him for compulsory support; and

Whereas, the party of the second part is willing to accept a satisfactory allowance properly secured, provided it is without prejudice to her legal rights based on the conduct of the party of the first part;" (R. 45.)

"Third: The party of the first part hereby agrees to assign and transfer unto the Trustee, and at all times to keep and maintain in the hands of the Trustee good, valid and marketable securities of a market value which shall at no time bear and yield an annual income of less than Twenty Five Thousand Dollars (\$25,000)." (R. 46.)

"Fourth: * * *

(a) That the Trustee shall during the life of the party of the first part, receive and collect the interest, income and dividends upon the said securities, and upon any other or substituted securities that may be transferred and delivered to it as hereinafter provided, and shall pay over the same to the party of the second part quarterly, or semi-annually, as the same are collected, during the lifetime of the party of the second part. If in any year the said interest, dividends and income so paid shall exceed the amount of Twenty Five Thousand Dollars (\$25,000) the surplus shall be

paid to the party of the first part or his legal representatives. Provided, however, that if the party of the second part shall meantime have procured an absolute divorce from the party of the first part and shall have remarried, from and after such remarriage there shall be paid to her out of the interest, dividends and income from such securities or from any substituted securities, the sum of Fifteen Thousand Dollars (\$15,000) per annum, and no more, and in such event the entire surplus of income over and above said annual sum of \$15,000 shall be paid to the party of the first part or his legal representatives." (R. 48, 49.)

"(d) Upon the death of the party of the second part, the trusts hereby created except as to the aforesaid sum of \$150,000 above provided for, to be disposed of by the party of the second part by will, shall cease and determine, and all the remaining securities then in the hands of the Trustee, under the trusts hereof shall be transferred and paid over unto the party of the first part or his legal representatives, or as he shall direct by will or otherwise." (R. 49, 50, 51.)

"Sixth: If at any time during the existence of the trusts hereby created, there shall be a default in the payment of interest or dividends upon any of the securities then constituting a part of the trust estate hereby created, the party of the first part will forthwith, upon the demand of the Trustee, assign, transfer and deliver to the Trustee, in substitution for those securities defaulted, securities of a character approved by the Trustee, or by the party of the second part, which shall yield an income equal to that of the securi-

ties on which the default of interest shall have occurred, or with respect to which the dividends shall not have been paid. The failure or omission of any corporation the securities of which are to be held by the Trustee to pay its usual dividend at the time at which the same is ordinarily paid, shall constitute a default within the meaning hereof.

Seventh: If the securities forming part of the trust estate, shall in any one year yield unto the party of the second part an income of less than \$25,000, provided the party of the second part shall not meantime have married, or less than \$15,000, provided she shall have remarried, the party of the first part shall forthwith make good such deficiency by paying the amount thereof to the Trustee." (R. 51, 52.)

"* * * the intent hereof being to provide for the party of the second part *such support* as she would be able to enforce, but for the provisions hereby made. No judgment or decree of divorce hereafter procured by the party of the second part, shall in any way invalidate or affect the trusts of this agreement." (R. 55.)

"* * * provided, however, that the net annual income, payable from said estate to the party of the second part, shall be at no time less than the amounts above fixed, and the party of the first part shall make good any deficiency in the said income, including therein the expenses of the administration of this trust." (R. 56.)

"Nineteenth: This agreement shall bind the respective heirs, executors and legal representatives of the parties of the first and second parts." (R. 57.)

On October 1, 1906, in South Dakota, the wife obtained an absolute divorce. The divorce decree is Exhibit 2 of the stipulation. It specifically denied alimony. In that respect it was final. (*Cameron v. Cameron*, 31 S. D. 335, 140 N. W. 700.) (Item 3, R. 39 and 57.)

The ex-wife never remarried. (Item 4, R. 39.)

James F. A. Clark died December 9, 1939 and Central Hanover Bank and Trust Company became his executor. (Item 7, R. 39.)

Estelle P. Clark died September 19, 1937 a resident of Alameda County. Her will attempted to exercise the power of appointment reserved in subparagraph (b) of Par. Fourth of the agreement but the validity of the exercise of the power is under attack. (Item 8, R. 39 and 40.)

The petitioners herein are the executors of the will of Estelle P. Clark. (Item 9, R. 40.)

In his lifetime, James F. A. Clark substituted good securities for defaulting held under the agreement of February 28, 1906, and he directed changes in the trust securities. (Item 11, R. 41.)

On June 23, 1937, the trustee under the trust agreement obtained a judgment against the estate of James F. A. Clark for \$4040.06, as income deficiency under the trust for the year ending July 7, 1936. The suit in which the judgment was rendered was brought also for the purpose of obtaining construction of the agreement and to have the trustee's account settled. Defendant appealed from the said judgment, but

"Following the death of decedent which occurred on September 19, 1937, said appellant withdrew its appeal and said judgment is now final." (Item 12, R. 42, mid-page.)

This judgment provided:

"Ordered, Adjudged and Decreed that it was the intention of the said James F. A. Clark and Estelle P. Clark, that the covenants and provisions contained in the said agreement should be binding upon their respective executors and administrators; and it is further

"Ordered, Adjudged and Decreed that the rights and obligations of the respective parties to the agreement of February 28, 1906, were intended by the parties to be in lieu of and in substitution for any and all obligations resting upon said James F. A. Clark for the maintenance or support of Estelle P. Clark;" (R. 102.)

At the death of Mrs. Clark on September 19, 1937, the securities in the trust exceeded in value \$400,000.00. In some years the trust income exceeded \$25,000.00. This excess was paid to Mr. Clark. (Item 13, R. 42 and 43.)

The divorce decree shows that the divorce was absolute and that no alimony was allowed. (Item 14, R. 58 to 60.)

The Court will observe that in the agreement of February 28, 1906, there was no disposition of the reversionary interest in this trust. There could be no change in the securities held by the trustee except as directed by James F. A. Clark although it was re-

quired that either the trustee or Mrs. Clark should consent. This right was reserved on behalf of James F. A. Clark and his estate. (See Par. Tenth, R. 53.)

Moreover, the agreement expressly stated in Par. Fifteenth that the trustee should be in no respect responsible for investments. (R. 55.)

It was stipulated:

“He made good deficiencies when the income of the trust was less than \$25,000 for any fiscal year ended July 7, as provided in the Seventh paragraph of said agreement and from time to time he made changes in the securities included in the trust with the consent of the trustee or the decedent, as provided in the Tenth paragraph of the agreement.” (R. 41.)

IMPORTANT QUESTIONS INVOLVED.

The Court should grant a review in this case in order to have correctly answered the following questions.

1. Whether the majority opinion below has not misapplied the *Pearce* case and created an illegal guide.
2. Whether the parties to this contract could give to the payments which were to be made to the wife after the husband's death the same character which they gave to the payments made before such death.
3. Whether the cases decided by this Court indicating these contracts are support contracts, although they may run beyond the husband's life, are in error.

4. Whether the *Alsop* case, the *Donnelly* case, the *Glendinning* case, *Weir* case, the *Barbour* case and the *Tilles* case, all indicating that by contract the parties can distribute the support payments over a period in which the making of support payments could not be compelled, are erroneous.

5. Whether the two New York cases on this point mentioned in the attached brief are in error.

6. Whether, if under local law where the contract was made the after-death payments are ruled to be for support, the Federal Courts should not so treat them.

7. Whether the death of the husband does in such a case as this convert that which was income of the husband into income of the wife.

8. Whether, if the contract to make the payments means it shall be binding upon the husband's estate if he dies first, there is any legal factor or any change in remedy that so alters the creditor-debtor-security arrangement as to require a holding that after the husband dies the income of the trust must be treated as income of the wife.

Whether, if there was a lien on trust corpus to secure income deficiencies we would not have a plain case of security.

9. Whether the Court below did not misapply the *Leonard* case and the law generally in holding that if all that the husband or his estate is liable for is to make up income deficiencies, the case is taken out of the case which hold that the income is taxable to the husband.

10. Whether, the Court below did not misconstrue the *Butterworth* case in saying, in effect, that the law intends the trust income shall be taxed as a unit.

11. Whether, the Court below did not misconstrue and misapply the Treasury Regulations governing the taxing of income on alimony trusts.

12. Whether the retention of the interest by the husband in the trust and his control over it did not at least create a doubt as to whether the trust was a trust to serve the husband's purposes.

THIS COURT HAS JURISDICTION.

Judicial Code, Section 240(a);

28 *U. S. C. A.*, Section 347(a);

Magnum Import Co. v. Coty, 262 *U. S.* 159,
43 *S. Ct.* 531, 67 *L. ed.* 922.

The brief will follow.

Wherefore, petitioners respectfully pray the writ of certiorari issue out of and under the seal of this honorable Court, directed to the Honorable Circuit Court of Appeals for the Ninth Circuit in San Francisco, requiring that Court to certify and send to this Court for its review and determination, on a day certain to be therein named, a full and complete transcript of the record and all proceedings in the case numbered 9879 on its docket and entitled "Stuart Daggett, Sr., and American Trust Company, Executors of the Last Will and Testament of Estelle P. Clark, Deceased, Peti-

tioners, vs. Commissioner of Internal Revenue, Respondent" and that the said decree of said Court may be reversed by this Honorable Court and that your petitioners may have such other relief in the premises as to this Honorable Court may seem meet and just.

Dated, Berkeley, California,
September 4, 1942.

NORTHCUTT ELY,
Attorney for Petitioners.

REECE CLARK,
GEORGE CLARK,
Of Counsel.



In the Supreme Court

OF THE
United States

OCTOBER TERM, 1942

No.

STUART DAGGETT, SR., and AMERICAN
TRUST COMPANY, Executors of the
Last Will and Testament of Estelle
P. Clark, Deceased,

Petitioners,

VS.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

BRIEF IN SUPPORT OF PETITION FOR WRIT OF CERTIORARI.

As we have discussed the cases dealing with alimony trusts, this brief will be confined to four points.

I.

Repeated rulings under the Bankruptcy Act show there is no objection to the husband's agreeing to

make the support payments in any reasonable period fixed by the parties. Death may intervene but the payments agreed to are still support payments.

II.

The creditor-debtor-security arrangement which was created by the contract of February 28, 1906 continued after the death of James F. A. Clark on September 9, 1935.

The continuance of the security arrangement and of the debt is emphasized by the fact that the contract conferred a lien on trust corpus for unpaid income deficiencies.

III.

That the wife waives her contingent dower right does not prevent but rather invites treating the payments as alimony. (In *Douglas v. Willcuts* the wife waived dower.)

The power of appointment was not property and in any event the payments were for support. (In the *Leonard* case, the wife received a power to appoint.)

IV.

The husband remained continually interested in the trust and had a large control over it. The same interest and the same control continued in his estate. The arrangement survived his death.

I.

REPEATED RULINGS UNDER THE BANKRUPTCY ACT SHOW THERE IS NO OBJECTION TO THE HUSBAND'S AGREEING TO MAKE THE SUPPORT PAYMENTS IN ANY REASONABLE PERIOD FIXED BY THE PARTIES. DEATH MAY INTERVENE BUT THE PAYMENTS AGREED TO ARE STILL SUPPORT PAYMENTS.

If the payments which the husband has promised to make to his wife in consideration of his duty to support her happen to fall due *after the wife dies*, the quality of the payments is not erased by the wife's death. Bankruptcy will not discharge the payments.

"The appellant asserts that the contract cannot be regarded as an agreement for the support of the wife because, upon her death, it inures to the benefit of her estate. But, unlike alimony, an agreement intended for support and maintenance need not terminate on the death of the party to be supported and maintained."

D'Andria v. Hageman, 253 App. Div. 518, 2 N. Y. S. (2d) 832, re-argument denied, 254 App. Div. 662, 4 N. Y. S. (2d) 376, affirmed, 278 N. Y. 360, 16 N. E. (2d) 294.

Note that the case marched through every Court of New York.

The following New York case presented an after-death demand for alimony. The issue of discharge in bankruptcy was not directly involved but the Court of Appeals took occasion to say the wife was a creditor and the claim could not have been discharged in bankruptcy. The reference was to the tag end due *after the husband died*.

“The separation agreement was for her maintenance and support. The debt was not dischargeable in bankruptcy. Matter of Ridder, 2 Cir., 79 Fed. 2d 524, 103 A.L.R. 719. As such creditor she was preferred over general legatees and annuitants.”

In re Bloomingdale's Will, 278 N. Y. 435, 17 N. E. (2d) 121, modifying decrees of Appellate Division, 252 App. Div. 563, 300 N. Y. S. 499, reargument denied, 253 App. Div. 798, 1 N. Y. S. (2d) 1015.

These cases are founded on Federal Court rulings which show that in agreeing upon payments to be made to a wife for her support, the parties are not, in fixing times of payment, governed by what a divorce court might order.

Section 17 (U. S. C. Title 11, Sec. 35) of the Bankruptcy Act now *expressly* provides that payments agreed to be made by a husband in consideration of his obligation to support his wife shall not be discharged in bankruptcy. The amendment of February 5, 1903 (32 Stat. at L. 797) merely clarified the law. This is shown in *Wetmore v. Markoe*, 196 U. S. 68, 49 L. ed. 390. The question arose in the Federal Courts as to whether, if these payments are to be made in a period when the payment thereof could not have been required by the Court's decree in a divorce action, they come within the law's favor. We have mentioned the concurring opinion that Judge L. Hand rendered in the *Thomas* case and stated the Judge had in mind

his prior opinion in the bankruptcy case of *In re Adams*, 25 F. (2d) 640. There the husband and wife were residents of New York. They made their separation agreement on October 1, 1920. It provided for maintenance of the wife until she remarried or *until she died*. The husband divorced the wife for her adultery, the decree being entered June 3, 1921. He was later adjudicated a bankrupt. He had quit paying under the agreement in 1923. The wife died in 1925. Suit was filed on the contract. The question was as to whether certain payments due after the default and after the divorce and before the wife died could be called maintenance and were discharged by the husband's bankruptcy. It was admitted that the Court could not and did not award the wife alimony, but the question remained as to whether the husband's liability to support the wife at the time of the pre-divorce agreement was not consideration for the payments involved and whether they were support payments. No question of good faith was involved. It was held:

"The fact that the parties chose to spread their payments over a period which might, if the suit proved successful, pass beyond the time when any such duty would exist presumptively affected the amount. Even so, those that fell due after the divorce *did not lose their character as liabilities for maintenance and support*. They were similar to a provision in a separation settlement *which might defer certain installments until after the death of the wife.*"

In re Adams, 25 F. (2d) 640.

Compare that with the Judge's statement in the *Thomas* case.

The Court then dealt with the uncertainties of such a bargain and refused to hold that such a contract rests on "complaisance". It held that the claim would not be discharged in bankruptcy.

In the following New York case the agreement was not set out but the Court said it was similar to the agreement in the *Adams* case. It was held that the contract to support was not discharged in bankruptcy although the agreement showed that it incidentally settled a suit for alienation of affections, *there being no showing that this affected the amount of the support payments.*

In re Ridder, 79 F. (2d) 524. (Certiorari denied, *Ridder v. Ridder*, 56 S. Ct. 599, 297 U. S. 721, 80 L. ed. 1005.)

The Eighth Circuit explicitly ruled that a note taken in consideration of the husband's obligation to support his wife was not discharged in bankruptcy; the payments were "maintenance" payments.

Blackstock v. Blackstock, 245 F. 249.

In the following case the Court made a like ruling. A note was executed by the husband in consideration of the maintenance duty. *The wife had died.* Before death she had accelerated the due date of the note pursuant to its terms relating to defaults. *Certainly the case shows that the payments to a wife for maintenance need not be continuously proportionate to the*

immediate wants of the wife or to the husband's present ability to pay.

In re Runge, 25 Fed. Supp. 31.

That the quality of these payments as support payments survived the death of the husband is shown by this Court's earlier rulings.

In *Dunbar v. Dunbar*, 190 U. S. 340, 47 L. ed. 1084, the husband was about to sue for a divorce. He promised he would make a contract to provide support for her and the children. She was without fault. She apparently had no counsel. The husband took a divorce decree by default and alimony was not mentioned. Then he made a written agreement to support his wife, which agreement was later amended. *The payments to the wife were to run for her life.* He had a change of heart and went into bankruptcy. He claimed the obligation rested on contract only and that it was not a case of alimony and that the demand was dischargeable. The argument that there was collusion was rejected. It was held that the husband's agreement was valid. The contract contained a clause that the payments should cease if the wife remarried. The Supreme Court found it unnecessary to determine whether this contract was dischargeable in bankruptcy because it was a contract to provide the wife with support. The decision was rendered before *Douglas v. Willcuts*. Nor did the Court answer: Did local divorce law discharge him because the decree failed to mention alimony? It held that because of the provision that payments should terminate if the wife remarried, the value of the contract could not be meas-

ured in bankruptcy; that it was too contingent to be subject to discharge. But the Court made this significant statement:

“The facts appearing in this record do not show a case of any moral delinquency on the part of the wife, and the contract, considering the circumstances, *might possibly be held to take the place of an order or judgment of the court for the payment of the amount*, as in the nature of a decree for alimony. We do not find it necessary, however, to decide that question in this case, because, in any event, we think the contract as to the support of the wife is not of such a nature as to be discharged by a discharge in bankruptcy.”

Dunbar v. Dunbar, 190 U. S. 340, 47 L. ed. 1084 at p. 1090.

In the case of *Wetmore v. Markoe*, 196 U. S. 68, 49 L. ed. 390, it appeared that the wife had in 1892 obtained a New York divorce decree requiring her husband to pay to her for her support \$3000.00 per annum *so long as she should live* and that he should also make payments for the support of the minor children. About \$20,000.00 in arrears had accrued under the judgment when the husband was adjudicated a bankrupt on January 13, 1899. Because of the then existing New York decisions, the decree was treated as an unchangeable alimony decree. On that ground the husband claimed that the judgment was but the equivalent of an ordinary contract; that as the decree became unchangeable, the foundation for it, the duty to support, was to be disregarded; that this duty was

merged in the judgment, that a judgment, while involuntary, but equals a contract debt. Later as is shown in *Helvering v. Leonard*, 310 U. S. 80, 84 L. ed. 1087, it was ruled in New York that an alimony decree was subject to change. But when *Wetmore v. Markoe* was decided, the United States Supreme Court was forced to declare exactly the opposite. But the Court ruled that the amounts payable under the Court's decree were not subject to discharge in bankruptcy. *While they ran for the life of the wife*, there was not the slightest indication that any part of this alimony judgment was dischargeable; that is, that the part of it that would be in effect if the husband died was not dischargeable. It said of the New York cases:

“These cases do not modify the grounds upon which alimony is awarded, and recognize that an alimony decree is a provision for the support of a wife, settled and determined by the judgment of the court.”

Wetmore v. Markoe, *supra*.

Note that the Supreme Court did not, as it did in *Dunbar v. Dunbar*, give any consideration at all to the question as to whether an ordinary annuity could be measured and discharged in bankruptcy. It certainly is the law that it is dischargeable. The Court would measure the obligation by tables employed by insurance companies which sell annuities. It would thereby be determined whether the wife would outlive the husband and if she would, the Court might fix the present worth of the part of the payments that would be payable after the death of the husband. It would seem,

that the extent of this part of the debt, the wife would share pro rata in the bankrupt's assets.

After the decision in *Wetmore v. Markoe* it was determined in New York in the case of *Wilson v. Hinman*, 182 N. Y. 408, 75 N. E. 236, 2 L. R. A. (N. S.) 232, that in the event the husband *did not consent to the decree* which would be effective after his death, such part of the decree would be void, but the Court took pains to point out that if the husband consented to the decree, the after-death alimony obligation provided for in the judgment would be unalterable. The Court said:

"It may very well be that by the agreement of the parties alimony might be *awarded in a different form* from that provided for in the statute; that is to say, the parties might agree that a gross sum should be paid as alimony or that an allowance should be made to the wife which would bind the husband's estate after his death. *An agreement of that character would in no way contravene public policy and the performance of it would doubtless be enforceable by the courts.* It is on this ground that the decision in *Storey v. Storey*, 125 Ill. 608, 18 N. E. 329, 1 L.R.A. 320, 8 Am. St. Rep. 417, proceeded."

Wilson v. Hinman, 182 N. Y. 408, 75 N. E. 236, 2 L.R.A. (N. S.) 232.

Such a contract though *for life* was formerly a complete substitute for the Court's action and if made, precluded the making of a decree for support in the divorce action.

Galusha v. Galusha, 116 N. Y. 635, 22 N. E. 1114, 6 L.R.A. 487.

II.

THE CREDITOR-DEBTOR-SECURITY ARRANGEMENT WHICH WAS CREATED BY THE CONTRACT OF FEBRUARY 28, 1906 CONTINUED AFTER THE DEATH OF JAMES F. A. CLARK ON SEPTEMBER 9, 1935.

In the following New York case it was ruled that where the separation agreement contained a provision entitling the husband, in the event of his death, to secure the support payments by setting up a trust in his estate and where the husband did create such a trust by his will, the rights which the wife could assert through this trust were the rights of a creditor.

In re Fuller, 271 N. Y. S. 685, affirmed 242 App. Div. 623, 271 N. Y. S. 1099.

It is familiar practice to allow a remedy to the holder of a contingent liability against an estate. Where the wife holds a husband's contract to provide her with support for life and he dies, the Court impounds so much of the husband's estate as is necessary to meet payments which *may* fall due.

Barnes v. King, 129 App. Div. 192, 113 N. Y. S. 325.

Like practice prevails in California when the claim presented calls for payments that are uncertain in amount.

Joost v. Castel, 33 Cal. App. (2d) 138, 91 Pac. (2d) 172 (hearing denied by Supreme Court).

Dabney v. Dabney, 9 Cal. App. (2d) 665, 51 Pac. (2d) 108.

No civilized jurisdiction cuts off the creditor's rights against the debtor's property because of death. If

there is an existing debt and if under existing probate law there is a means of proving the claim, and the legislature does by a new law so clog the remedy as to make the debt worthless, the law will violate the contract clause. After a debt was created under a law that allowed proof of claim against an estate by affidavit, the legislature of Arkansas passed a law forcing the holder of an estate claim, no matter how petty, to appear in Court and support the same by his oath. This made small claims worthless. The law was held to be invalid. The Court said:

“The legislature certainly does not have the power to cut off all demands against the estate of a deceased person or so to impair the right or clog the remedy as to render it inoperative or valueless.”

Riggs v. Martin, 5 Ark. 506, 41 Am. Dec. 103.

Where proceeds of a life insurance policy are not exempt from execution and such proceeds may under an existing law be reached in the event of the death of the debtor, the legislature cannot as against an existing debt amend the law so as to exempt such insurance monies. A Federal case was cited.

Estate of Heilbron, 14 Wash. 536, 35 L.R.A. 602.

As shown in Restatement of the Law of Trusts (American Law Institute) the wife had a lien here on what the trustee held to the extent necessary to cure the husband's defaults. On that ground also a usual remedy against the husband's property survived. The contract here was continuously executory. The husband and his estate had to supply paying securities for

those that defaulted. We quote from the work referred to.

"252. Covenant by One Beneficiary to Pay Money Into the Trust.

"If one of the beneficiaries of a trust contracts to pay money to the trustee to be held as a part of the trust estate and he fails to make the payment, his beneficial interest is subject to a charge for the amount of the liability.

Comment:

(a) If a person transfers property in trust for himself and another and covenants to pay an additional sum to the trustee to be held upon the same trust, and he fails to make the payment, his interest in the property is subject to a charge for the amount by which he is in default. He is not entitled to receive his share of the trust property without making good the default or without deduction from his share of such amount.

Illustration:

By a separation agreement between A, a husband, and B, his wife, A transfers certain securities to C in trust to pay the income to B for life and on her death to pay the principal to A. By the agreement A covenants to pay \$10,000 within a year to C to be held upon the same trust. A fails to make the payment for four years after it is due. B dies, B's personal representatives are entitled to a charge upon the trust property for the amount of interest by which A is in default."

Restatement of the Law, Trusts, Sec. 252.

In Tentative Draft No. 4, of the article, this section was Section 244. The annotations under said section cited:

In re Weston (1900), 2 Ch. 164.

As shown by the first page of Tentative Draft No. 4, the reporter on the article had 14 advisers, part of them of New York City. (See first page of Draft No. 4.)

In the case cited, the Court said:

"In truth, however, the right in its strictest form, appears to be wider than is admitted by the assignee in bankruptcy; it is that a person entitled to property legally vested in a trustee cannot compel those trustees to hand over the property to him until he has satisfied a debt due to those trustees and arising under the instrument which creates the trust."

In re Weston, 2 Ch. D (1900), pages, 173-174.

By law and by contract, the guarantee remained enforceable. The power of appointment could be surrendered at any time.

Merrell v. Lynch, 13 N. Y. S. (2d) at page 514.

III.

THAT THE WIFE WAIVES HER CONTINGENT DOWER RIGHT DOES NOT PREVENT BUT RATHER INVITES TREATING THE PAYMENTS AS ALIMONY. (IN DOUGLAS v. WILL- CUTS THE WIFE WAIVED DOWER.)

THE POWER OF APPOINTMENT WAS NOT PROPERTY AND IN ANY EVENT THE PAYMENTS WERE FOR SUPPORT. (IN THE LEONARD CASE, THE WIFE RECEIVED A POWER TO APPOINT.)

We have discussed dower and have urged that the fact the wife strips herself of this right or that a property settlement is involved does not affect the character of payments which the parties have agreed are for support. We have mentioned that this point is met by *Douglas v. Willcuts* and by the specific terms of this contract and of a judgment.

The following New York case declared that the New York legislature deemed dower rights uncertain and illusory and that for that reason they in 1929 amended the law so as to require that a wife inherited a share in her husband's estate to the extent the will did not give her that share.

In re Jackson's Will, 31 N. Y. S. (2d) 54.

So dower right, at least in New York, was abolished before the husband died. So if we are to emasculate a simple provision of the contract, we have another question affecting value.

It is elementary that a power to appoint creates no estate in the donee of the power. In the *Fuller* case, the wife was given a power to appoint. (310 U. S. 69.) That did not affect in the slightest the decision as to the character of the weekly payments. There is perhaps some conflict in the law as to what jurisdiction

may govern the exercise of a power to appoint that is granted by the resident of a particular place, but there is no uncertainty whatever in the cases as to whether a power to appoint is property of the donee. It cannot be levied upon. It cannot be sold. Nothing can be realized out of it and if it is exercised, the gift under it is treated as the gift of the donor of the power. The power ordinarily takes effect by relation as of the date of the creation of the power and as a part of the instrument which creates it. The rule against perpetuities ordinarily applied requires that the limitation of suspension of vesting shall be measured from the date of the instrument which creates the power. The exercise of the power by Mrs. Clark's will is under attack. (R. 40.) While the Federal Estate Tax Law does impose a tax in the event a general power of appointment by will is exercised, it is not only early common law but the law as laid down in the decisions of the various states that a power to appoint is not property. This is declared in the following citations:

United States v. Field, 255 U. S. 259, 65 L. ed. 617 at page 620;

Estate of Bowditch, 189 Cal. 377, 380.

"* * * nor does a power of itself give the donee or grantee any interest or estate in the property."

49 *Corpus Juris* 1276.

The general rule that a power to appoint is not property is qualified in England and in some states to this extent: If a general power to will is exercised and the donee leaves debts, the creditors may seize the gift.

Shattuck v. Burrage, 229 Mass. 448, 451, 118 N. E. 889.

That is not the rule in New York.

Cutting v. Cutting, 86 N. Y. 522.

The conclusion simply would not be sensible that granting the power to appoint *increased* the support payments.

IV.

THE HUSBAND REMAINED CONTINUALLY INTERESTED IN THE TRUST AND HAD A LARGE CONTROL OVER IT. THE SAME INTEREST AND THE SAME CONTROL CONTINUED IN HIS ESTATE. THE ARRANGEMENT SURVIVED HIS DEATH.

This point was at no time waived although we stressed the first point. It was stipulated that the changes in the investments in the trust were at the direction of the trustor. (Item 11, R. 41. See Par. Tenth of agreement, R. 53.)

In the following case the husband created a trust which would continue for five years unless the husband or the wife died. It was provided that all income should be for the wife's exclusive benefit and that she should be entitled to all gain from investments of trust income. The husband could pay out the trust income to the wife in his discretion. The husband could control the trust investments and he was given wide discretion in the management of the trust. He reserved the right to the trust corpus. This court held that the trust was the husband's trust for the purpose of the income tax law.

Helvering v. Clifford, 309 U.S. 331, 84 L. ed. 788.

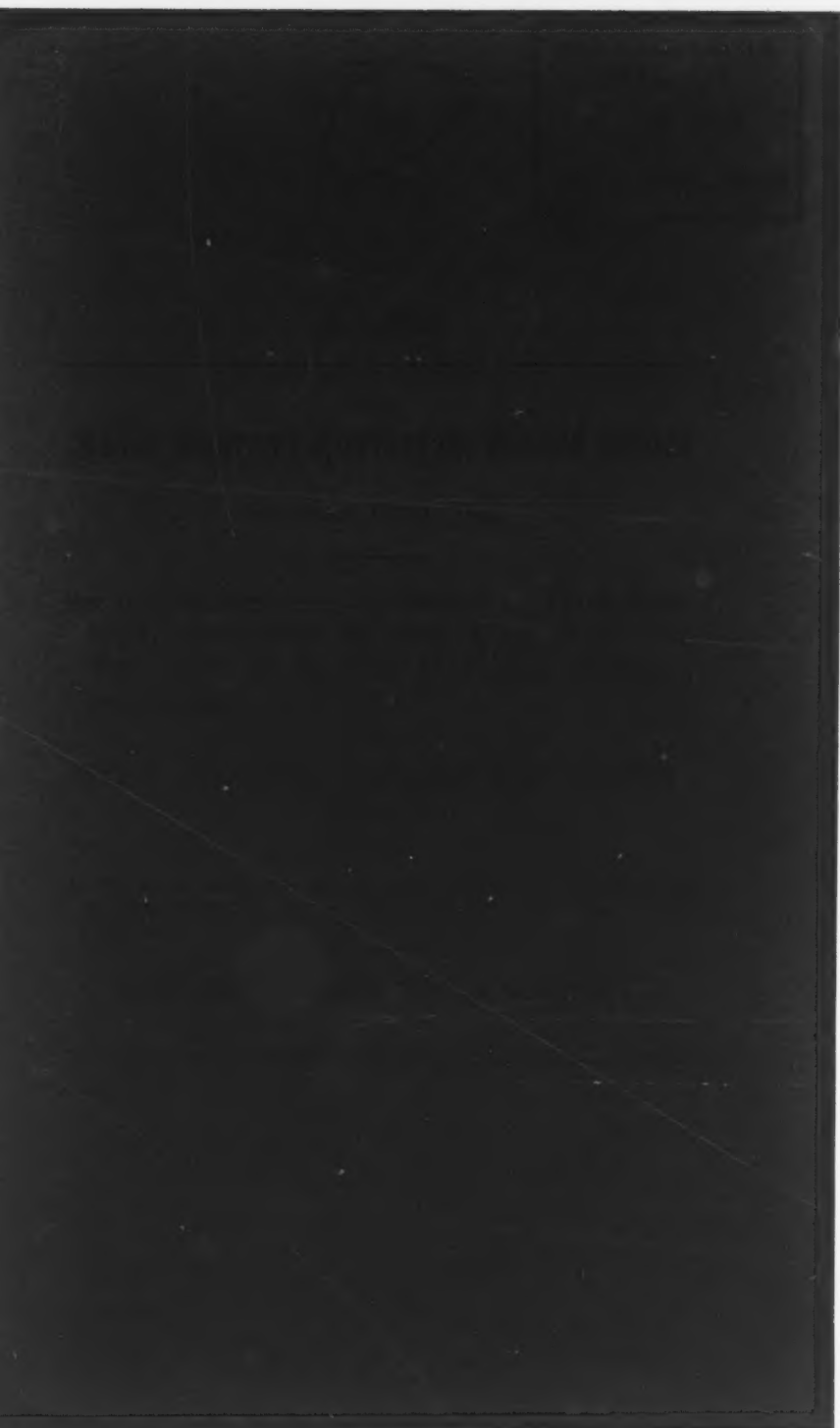
The trust instrument here starts out by saying that the wife is willing "to accept a satisfactory allowance properly secured", etc. (R. 45, mid-page.) Obviously, the main purpose of the agreement was to create a type of a mortgage to serve a purpose of the husband. Securities could be changed only at the instance of the husband although the trustee or the wife had to approve. (Par. Tenth, R. 63.) But the instrument recited that the trustee was in no way responsible for the management of the trust. (Par. Fifteenth, R. 55.) The trustor was to receive annually all income above payments to the wife. (Par. Fourth, Subdiv. (a), R. 48.) Capital gains were his. Except for the fact that the husband granted to the wife a power of appointment, the court should not hesitate to call this trust a mere security device. However, the creating of a trust is not necessary to the creation of a power of appointment. All that is necessary is that there shall be a vested estate to which the power is by some instrument attached. In *Helvering v. Clifford* the wife had an interest in the trust because the entire income was conferred upon her. We contend that the majority of the important features of the trust before the court justifies classing it as the husband's trust; a trust to serve the husband's purpose.

Dated, Berkeley, California,
September 4, 1942.

NORTHCUTT ELY,
Attorney for Petitioners.

REECE CLARK,
GEORGE CLARK,
Of Counsel.







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(1)



In the Supreme Court of the United States

OCTOBER TERM, 1942

No. 392

STUART DAGGETT, SR., AND AMERICAN TRUST COMPANY, EXECUTORS OF THE LAST WILL AND TESTAMENT OF ESTELLE P. CLARK, DECEASED, PETITIONERS

v.

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE NINTH CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

OPINIONS BELOW

The opinion of the Board of Tax Appeals (R. 21-26) is reported in 44 B. T. A. 32. The opinion of the Circuit Court of Appeals for the Ninth Circuit (R. 110-133) is reported in 128 F. 2d 568.

JURISDICTION

The judgment of the Circuit Court of Appeals was entered on May 28, 1942, and the order denying petition for rehearing on July 15, 1942 (R.

133-134). The petition for writ of certiorari was filed on September 11, 1942. The jurisdiction of this Court is invoked under Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTION PRESENTED

The decedent's divorced husband, also deceased, created a trust prior to their divorce in order to satisfy her claim for support and for dower. The question is whether she was liable, under the provisions of Section 162 of the Revenue Act of 1936, for income tax on amounts received by her from the trust after her former husband's death.

STATUTE INVOLVED

Revenue Act of 1936, c. 690, 49 Stat. 1648:

SEC. 162. NET INCOME.

The net income of the estate or trust shall be computed in the same manner and on the same basis as in the case of an individual, except that—

* * * * *

(b) There shall be allowed as an additional deduction in computing the net income of the estate or trust the amount of the income of the estate or trust for its taxable year which is to be distributed currently by the fiduciary to the beneficiaries, and the amount of the income collected by a guardian of an infant which is to be held or distributed as the court may direct, but the amount so allowed as a deduction shall be

included in computing the net income of the beneficiaries whether distributed to them or not. Any amount allowed as a deduction under this paragraph shall not be allowed as a deduction under subsection (c) of this section in the same or any succeeding taxable year;

* * * * *

STATEMENT

The facts were stipulated and were summarized by the Board of Tax Appeals as follows (R. 22-23):

A trust was created in 1906 by the decedent's former husband in connection with an agreement which the parties made in contemplation of their separation, and in consideration of a release by the decedent of all claims against her husband and his estate for her support and that of their child during the latter's minority. The husband agreed "at all times to keep and maintain in the hands of the Trustee good, valid and marketable securities of a market value which shall at no time bear and yield an annual income of less than Twenty Five Thousand Dollars (\$25,000)." The trustee was to pay this amount of income to the wife annually for life (or after her remarriage, \$15,000), and to pay any excess income to the husband. In case of a deficiency in trust income, the husband agreed to pay the difference to the trustee. The wife was given the right to dispose by will of trust corpus of \$150,000; upon her death, remaining corpus was to re-

vert to the husband. Husband and wife mutually released curtesy and dower rights in realty owned by each (R. 22).

On October 1, 1906, the decedent procured an absolute divorce in South Dakota. After adverting to the fact that suitable provision had been made for her support and the daughter, the court decreed "that no allowance be made the plaintiff for alimony, support or maintenance, and that in this respect this decree shall be final and not subject to future modification or amendment" (R. 23).

The trust was carried out; the decedent never remarried, and prior to 1930 the daughter attained her majority. The husband died on December 9, 1935. The decedent died on September 19, 1937, a resident of California since 1930. She disposed by will of \$150,000 of the trust corpus, and such appointment is now the subject of litigation. During the husband's life, he made good deficiencies in trust income when it was less than \$25,000. For the fiscal year of the trust ending July 7, 1936,¹ there was a deficiency of \$4,040.06, which the decedent's executors have recovered from the trustee by a judgment of the Supreme Court of New York, entered June 23, 1937, in which it was (R. 23):

"Ordered, Adjudged and Decreed that the rights and obligations of the respective

¹ The Board's opinion erroneously gives the date as July 7, 1937. See Stipulation R. 41. It is shown elsewhere that this deficiency occurred prior to the beginning of the calendar year 1936. See R. 72, 92.

parties to the agreement of February 28, 1906, were intended by the parties to be in lieu of and in substitution for any and all obligations resting upon said James F. A. Clark for the maintenance or support of Estelle P. Clark; * * *

During the husband's life, amounts distributed to the decedent out of income of the trust were excluded from her taxable income; but the Commissioner has now held that upon his death she became the sole beneficiary of the trust and liable under Section 162 (b), Revenue Act of 1936, for tax upon the distributable income (R. 23-24).

The Board approved the Commissioner's determination and found that the decedent owed deficiencies in income tax in the amounts of \$2,365.06 for 1936 and \$1,149.14 for the portion of 1937 expiring before her death on September 19, 1937 (R. 26.)

ARGUMENT

The decision below is in accord with *Thomas v. Commissioner*, 100 F. (2d) 408 (C. C. A. 2d), and there are no decisions to the contrary.

Section 162 (b) of the Revenue Act of 1936, *supra*, requires a beneficiary to whom trust income is currently distributable, as in the instant case, to include such income in computing such beneficiary's net income for tax purposes. Under this section Mrs. Clark would be liable for tax on the trust income distributed to her as beneficiary of the trust created by her husband prior to their divorce. Cf.

Helvering v. Butterworth, 290 U. S. 365. However, it is contended that this is a case for application of an exception to the general rule, namely, that where trust income is payable to a divorced wife as alimony under the divorce decree, it is taxable to the divorced husband. *Douglas v. Willcuts*, 296 U. S. 1; *Helvering v. Leonard*, 310 U. S. 80; *Helvering v. Fitch*, 309 U. S. 149. And it is pointed out that the husband did pay tax on this trust income during his lifetime. The contention is without merit here because this case involves the period *after* the husband's death. The obligation to pay alimony terminated at his death, with the consequence that the trust payments thereafter were not in discharge of any continuing obligation and must therefore be included in the income of the recipient in the usual course.

In none of the income tax cases cited by petitioners had the husband died. Moreover, while in several of these cases the trust income was made payable to the divorced wife for life, there is no suggestion in any of the cases indicating that the wife's exemption from tax should continue after the husband's death.

Pearce v. Commissioner, 315 U. S. 543, did not involve a situation where the husband had died. However, the decision makes it clear that the showing which a divorced wife must make to avoid the tax bears upon the question whether the personal obligation of her husband is being satisfied by the

payments made to her. The death of the husband precludes such a showing here.

CONCLUSION

There is no conflict, and the decision of the court below is in accord with established principles. The petition should be denied.

Respectfully submitted.

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